

## **The Traditional Contract System - It's Role to the Development of Small Scale Palm Sugar Industry in Bengkulu**

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### **ABSTRACT**

The small scale palm sugar industry is having significant contribution to strengthen rural economics' structure. Unfortunately, in rural area there is less developed transportation and communication network so as competitive market economy. Thus, the agent's in rural area is facing many barriers such as less price information, limited numbers of agricultural inputs both timely and spatially. As the result, the palm sugar agent creates another alternative exchange institution of the principle – agent type of relationship that dominated rural economy, even taking lower profit share. For that purposes, the study describes role of the contract system mechanism in the small-scale palm sugar industry. This research was conducted on July to Augusts 2011 by survey approach. The descriptive analysis was utilized to explaining the existence of traditional contract system.. There are four types of perennial crops, especially of palm used for sugar making between the tappers and the owners. The contract offers both guaranteed market and purchased price to tappers who have never had assurance. The evidences show the traditional contract system of small palm sugar industry supposed to be sustained a monopoly market.

**Key words:** traditional, contract system, palm sugar, small scale industry

### **INTRODUCTION**

Agricultural sector has been the main focus in Indonesia development strategy, because the land and labor were underutilized. Over the past two decades, the sector's notable contribution to reduce poverty and employment, significantly. In spite of significant contribution, the policy's was bias to the large agro-processing industry (Garcia, 2000; Wiyatiningsih, 2000). Consequently, the inability of policy makers in improving and accommodating all agricultural agents had negative effect on the foundation of the rural and agricultural economy, on which the majority of the population depends. Therefore, when the crisis hit, the large size agro processing industry was collapse and it takes wide spread unemployment in Indonesia.

The small-scale industry is palm sugar industry which is having bright prospect to be a leading sector and making significant contribution to Regional Income in forth coming. It means that the small-scale agro processing industry has some potential in create employment, alleviate poverty, reduce urbanization, and strength economic structure. Unfortunately, in rural area, there is less developed transportation and communication network so as competitive market economy. Thus, so the agent's far rural area is facing many barriers such as less price information, limited numbers of agricultural inputs both timely and spatially.

Consequently, the price doesn't function as the sufficient resource allocation coordinators. The performance of formal marketing institution like village cooperatives (KUD) was getting worst. If these conditions especially in rural economy would follows prescription based on the premise of the standardized competitive market economy, it could be missing market that causes great bias and efficiency loss (Monke and Eric, 1989). As the result, the palm sugar agent creates another alternative exchange institution of the principle – agent type of relationship that dominated rural economy, even taking lower profit share (Bardan, 1989; Sadoulet and Janvry, 1995; Anwar and Hermanto, 2001). Based on the previous description, the objectives of the study were to elaborate the role of traditional contract system in developing the small scale palm sugar industry in Rural Bengkulu.

### **MATERIALS AND METHODS**

In rural area such Air Meles Atas, Rejang Lebong District, Bengkulu Province was chosen as a research site because many villagers were engaged in palm sugar making. The area has a diverse

population with agricultural system farming cultivation, horticulture (vegetables) and palm sugar processing as main livelihoods. For the market and large variety of nonagricultural occupation was also exists. These include small-scale industries such as carpenter, house building, tailoring, trading, and servicing as well. Secondary data was collected from local government institutions. Primary data was collected of 30 households at Air Meles Atas, Rejang Lebong district. The data collected of interviews with each tappers. The questionnaire was designed to yield complete picture of each tappers (product, size of palm tree, credits, labor, range of demographic and background data), marketing, and traditional contract systems. The data was analyzed descriptively to depth explaining of existence of traditional contract system in palm sugar marketing in Rejang Lebong.

## **RESULTS AND DISCUSSIONS**

### **Marketing System of Palm Sugar**

The domestic marketing systems of palm sugar just comprise one market, but it has functions as both local and regional markets. The functions of a local market was a central palm sugar market and it may be at the village, and sub district or district level and most of them are scattered along the agents' place. This was a place where tappers and middlemen trade their commodities.

The regional market was also at the same place for delivering palm sugar to other cities or provinces. The tappers fully supplied to the village's middlemen, and the village's middlemen fully supplied to the sub district/district's middlemen. The sub district's middlemen completely distribute it to local and regional foods industries, local and intercity wholesalers and supermarket. The raw material mostly locally while the market orientation mostly outside.

The total of palm sugar which is delivered to regional market (75 percent) was to South Sumatera (Palembang, Lubuk Linggau), Bengkulu, and local uses (25 percent) in terms of direct consumption, raw material of sauce, and other products. The exports market is delivered through the intermediaries from others cities/provinces. The major's orientation of the export market was to Singapore, Malaysia, Europe, and Middle-East. In principle a fully efficient marketing system is one which moves goods from producers to consumers at the lowest possible cost consistent with the provision of the services that producers and consumers desire (Azzaino, 1983).

In long terms, the markets in production area to market area tend to integrate and competitive. The flow of price information functioning well as quality signal. In the short terms, the existing of asymmetric of the price information by traditional contract systems, then the price stabilization policy should be taken where was the structure of the palm sugar was less integrated (Monke and Eric, 1989; Azaino, 1981). Of course, each region needs the different strategy, because of uncommon response. The policy at district level may effect directly to development of local market include policies on distribution and price determination (Tambunan, 1992).

### **Traditional Contract in Palm Sugar Small Scale Industry**

The historical of Indonesian's traditional contract system had employed by community as well as the dynamic of the agricultural activities for more than 2000 years (Wignjosoebroto, 2002). The relationship among the members of community is not only base on economic motives but also religious, political, social, cultural motives. The forms of these relations could be ranked in continuing of the vertical integration. Started from the weakest relation between the tappers and the village's middlemen at traditional market to the tightest ones such traditional contract. At the colonized period, the contract between the lowest class and the uppers class (called; the landlords) had established where the local people had deployed their control on private lands to the community rights. Through the head of the village, even though the contents of the contract was unexpected. The trust building among of them was the strongest. So, the local's offered their business to the principle.

Today's such contract shifted in the agent even unchanged the substantives. Ones of the common contracts are between the tappers (principle) and the middlemen (agent) in palm sugar industry at rural area in Rejang Lebong districts. Historically, the economic relations among of them were strong institutionalized. In this study, of a traditional contract scheme, it focus on relationships between tappers and middlemen in such contract. According to Oikawa (1998) in Indonesia, there are four types of usufruct of perennial crops in Indonesia. Those types were also found in specially of palm-sugar making between the tappers and the owners in Rejang Lebong, as follows : 1) Sharecropping is the

residents who don't have sufficient palm trees for sugar making can assure their living by sharecropping of palm trees or other contract types. The sharecropping is the most type of contract to use the palm trees owned by other villagers. Tappers harvest the owner's palm trees. For the next period, the tappers give all the production he harvests to the owner. These two periods are repeated alternately, 2) Paying per on or per kilo-an is In the case where a tappers pays on gram or kilograms, 3) Leasing is system where a tappers leases palm tree for a year and 3) Pawning is the contract where the owner pawns palm tree in unlimited terms, as long as the money was cashed yet.

### **The Relationship among the Actors**

#### **Tappers and Village's Middlemen**

In traditional contract scheme the middlemen plays significant contribution in providing credits to the tappers. They were provided two kinds of loans by the lenders both in kind and cash. These loan transactions appear to be extreme in their informality. They generally occur in private, with no witness and no written record. It was showed by preconditions should be fulfilled by borrower as 1) location, 2) familiar one each other's, 3) paying on palm sugar every market's days, 4) numbers of selling, 5) there is no fixed interest rate, and commodity price was determined on the market spot. The conditions imply that the tapper's feasibility not just depends on economics' but others resources feasibility such as trust, spatially engagement, and relatives/kinships.

The numbers of tappers who always were engaged in credit for consumption. They almost always made and repaid in kind or in cash. The fact that these transactions are loans, explicitly acknowledged and mechanisms exist that serve to enforce the implicit obligations of both parties. The tappers don't supply palm sugar to middlemen, sold palm sugar, and received loan from to extra middlemen were some defaults, which always occurred. But the fact shows that there was less tappers break down the negotiation. If could happen, the simplest and more directly penalty for default is exclusion of the defaulter from future opportunities to borrow from lender. The fact that these transactions occur within tappers and middlemen within the same villages permits mechanism for enforcing credit obligations through appeal to community. Reversibly, phenomenon could happen that community could tolerate their members whom received loan form others lender as well as not involved in last contract. The biggest loan, the best palm sugar price and the most in kind loan were backgrounds to shift the contract. The penalties rose as response to scarce of formal sanctions in traditional contract. Whereas the effective sanctions was enforced through community.

#### **Among the Village's Middlemen**

The relations between the village's middlemen not only base on economics' but also socials and local cultures in kinships and relatives. They are grouped in local institution called 'Arisan'. The establishment of it comes from uncertainty of the power of palm sugar market and common destiny. The price's information and transaction's mechanism were the main focus of the meeting. Because of the attractive palm sugar's market had permitted new agents to enter the markets, so as push competition among of them. There are some implications could be concluded from the meeting as follows: 1) to avoid unfair competition among of them who spatially near. If the best signal of the price raise, ones could get incentives to attract tappers sell their commodities to others, 2) to avoid moral hazards and adverse selections that could be raised by the tappers. It happens in terms of sell their product to or takes loan from other middlemen, 3) to strengthen the relationships in the terms of capital loans.

#### **Village's and Sub district's/District's Middlemen**

The common phenomenon which were happening between tappers and village's contract. It could happen in the contract relation between the Village's and the sub district's/district's middlemen. Both the preconditions and the penalties of the contract. They were provided two kinds of cash loans, namely forward and fixed cash and operational cash. Fixed cash is where the villages received cash range from hundred thousand to million rupiahs. Its use for attracting the middlemen's in the tightening contract. While operational cash is used to attract the tappers in a common contract. Besides, they could receive conditional loans such medical problems, tuition fee and consumptive acts. They almost always made and repaid in kind or in cash. The fact that these transactions are loans are explicitly acknowledge and mechanisms exist that serve to enforce the implicit obligations of both parties. More puzzling was the most lenders don't want to cash their loans, even the borrower was

offered the new ones. It would imply that there could be mechanisms to maintenance the contract and to minimize the risks, and to keep the supply continuity as well.

### **Implications of the Traditional Contract System**

In the most cases, the formal contract as well as the non-formal should cover explicitly or implicitly, the rights and the obligations for each of the parties. The formal contracts are scarcely take account for non-formal contract, as leads to uncompleted contract. The economic activity of the rural community could not separate ways from local characteristics, the absence of enforcement in formal contract criteria's were taken over by the roles of social and cultural relations. This type of contract would limit the flexibility of the borrower and lender in making the loan contract, but would economize on transaction costs and integrate well with the community-based enforcement mechanisms.

Even though the non-formal contract, however, these contract arrangements play an important role by minimizing risks, hazards and sharing revenues. The risks could be natural hazard, market risks and moral hazard. Most of the palm sugar agents, mainly the village and sub district or district middlemen could control the risks through the contract arrangements and the on - lending credits. The on-lending mechanism is the greatest loans divided into the smallest ones and the most parties. Besides, by diversifying its suppliers the middlemen can insulate itself against the risks; the tappers, however, is rarely in a position to diversify his/her buyers. The tappers/the lenders couldn't minimize the risks through this mechanism because it takes high transaction costs.

Finally, signing a traditional contract appears not as a choice but a necessity. The contract offers market guaranteed and (sometimes) purchase price to tappers who have never had assurance of either one. Tappers and a middlemen have accumulated not capital but debt since signing the contract. Some evidences show that the traditional contract system in palm sugar industry was supposed to be sustaining in monopoly.

Changing strategic environment of world trade under globalization, MEA/WTO/AFTA/APEC agreements, and more integration national's economic. Global phenomena were signed by high competition, standardization, specialization and high technology. It had diverse to whole sectors not only economic but also politics, social, culture etc. Meaning that national policy have to consider the world's changing. Globalization of agriculture had held since colonialization. The integration of agriculture sector under world trade system through global division of labor, commodity and raw material specialization by mean to satisfied the colonial. Today, almost two decade Trans National Corporation and Multi National Corporation agribusiness have significantly changed (Rustiani, 1997). They are shifting new investment to Less Developed Country, relaxing directly roles on-farm activities and signing contract to farmers and small scale industry.

Through market globalization can be built collaboration between small tapers and big business. This promises market integration, economic growth, transfer technology, protected taper's rights under contract and dynamic partnership. Even though promising the advantages, it doesn't always be taken by the tapers. Unfortunately, it causes some damage. Taking lesson from failure of agriculture contract system program such PIRBUN which was held by government's corporate. The affects were more gaps among tapers, unbalanced asset holding, imperfect information, unfair profit sharing and a risk that leads taper's position under pressure. The dependency traps them under monopoly and monopsony market. Both markets are always take place under such contract farming, because of dominancy asset by the big one. Noticing the descriptions, it needs anticipation programs through empowering mechanism so as restructuring institutional system. The process has to involve whole stakeholders ranging from the government, the investors and the NGO's, to the actors'.

### **The Policy Implications**

The economic activities of the palm sugar industry at rural area in Indonesia was feasible based on the comparative and competitive advantages. It is supported by the huge quantity of domestic resources i.e. labor, and raw materials. While the core agents face the limitation of the production equipment's. Therefore, it needs prudential consideration for future developed. Spatially, the palm sugar industries were distributed almost power of the tappers. Largely the practices of the traditional contract among the agent's leads to imperfect market caused incompletely transmit the price information. Therefore the economic rents just being enjoyed by the little agents namely middlemen not the tappers.

Future developing of the small-scale palm sugar industry in some rural area have to consider many aspects. The most significant are the continuity of raw materials, labors, and other resource endowments somewhat like culture, and experiences. These steps come true through integrated scheme, are improving land capability and capacity, new planting and rehabilitation local's estate. Empowering the actors under technical and managerial assistances. Creating fairly partnership mechanism through principle-agent institution. Lastly, the institutional mechanism need whole supporting from government whom constructing constructive incentives for investing. And also, out partner such non-government organization as a monitor.

## CONCLUSION

Government interventions are needed in creation of fairly mechanism in the local's market. It imposed through shifting the composition of the informal credits, not reducing even eliminating the roles of the informal agents in informal credit market. So as the market information's (the price information) freely flows to the tappers. Finally, it could rise the bargaining. It has to being considered by policy makers the idea of land consolidation of the tapers under one management. Where they were shifting their activities under professional manager whom is pointed by them. It just likes estate management which is held both government and public corporate.

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